9 T.C. 913 (1947)

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For excess profits tax calculations, deductions for employee benefits (premiums and pensions) are considered a single class; whether deductions are abnormal depends on consistent practice, and abnormality must not result from increased income or business changes.

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Summary

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Frank Shepard Co. sought to claim abnormal deductions for annuity premiums and pensions paid in 1938 and 1939 to reduce its excess profits tax. The Tax Court addressed whether these deductions were truly abnormal under Section 711(b)(1)(J) and (K) of the Internal Revenue Code. The court held that the deductions constituted a single class, were abnormal in 1938 due to their novelty, but were normal in 1939 because the company had initiated a consistent policy. Further, the court found that the abnormality was not a consequence of increased income or changes in the business. Thus, adjustments to the excess profits tax credit were required.

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Facts

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Frank Shepard Co., a publisher of legal citations since 1900, began providing employee pensions and annuity policies in 1938. Prior to 1938, the company had never offered such benefits. In 1938, facing the superannuation of older employees, the company pensioned two employees and purchased annuity policies for 21 others. It continued this practice in 1939, adding more employees to the annuity program. The company classified these expenses under a “Pension Roll” account, separate from regular compensation expenses. The company’s gross income increased in 1938 due to the publication of revised bound volumes.

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Procedural History

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The Commissioner of Internal Revenue disallowed the company’s claimed abnormal deductions for 1938 and 1939 when calculating excess profits tax. Frank Shepard Co. contested this disallowance in the Tax Court. The Tax Court addressed the proper classification and treatment of these deductions under relevant provisions of the Internal Revenue Code. The Tax Court ruled in favor of the taxpayer in part and against the taxpayer in part, determining that adjustments were required.

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Issue(s)

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1. Whether the deduction for premiums paid in 1938 was disallowable under Section 711(b)(1)(J)(i) and (K) as an abnormal deduction?

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2. Whether the deduction for premiums paid in 1939 was disallowable under Section 711(b)(1)(J)(i) and (K) as an abnormal deduction?

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3. Whether the deduction for pensions paid in 1938 was disallowable under Section 711(b)(1)(J) and (K)?

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4. Whether the deduction for pensions paid in 1939 was disallowable under Section 711(b)(1)(J) and (K)?

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Holding

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1. Yes, because the deductions for premiums and pensions in 1938 were a new and unusual expense for the company.

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2. No, because the company initiated a consistent course of conduct in 1938, making the 1939 deductions normal.

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3. Yes, in part, subject to limitations under Section 711(b)(1)(K)(iii).

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4. Yes, in part, subject to limitations under Section 711(b)(1)(K)(iii).

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Court’s Reasoning

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The court reasoned that deductions for premiums and pensions should be treated as a single

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